

Department of Health

**For the Year Ended
June 30, 2000**

Arthur A. Hayes, Jr., CPA, JD, CFE
Director

Edward Burr, CPA
Assistant Director

Ronald E. Anderson, CPA
Kandi B. Thomas, CPA
Audit Managers

Chris Risher
In-Charge Auditor

Jonathan Gebhart
LaToya Hampton
Temecha Jones
Roshena May
Staff Auditors

Amy Brack
Editor

Comptroller of the Treasury, Division of State Audit
1500 James K. Polk Building, Nashville, TN 37243-0246
(615) 741-3697

Financial/compliance audits of state departments and agencies are available on-line at
www.comptroller.state.tn.us/sa/reports/index.html.
For more information about the Comptroller of the Treasury, please visit our Web site at
www.comptroller.state.tn.us.



STATE OF TENNESSEE
COMPTROLLER OF THE TREASURY

State Capitol
Nashville, Tennessee 37243-0260
(615) 741-2501

John G. Morgan
Comptroller

April 25, 2001

The Honorable Don Sundquist, Governor
and
Members of the General Assembly
State Capitol
Nashville, Tennessee 37243
and

The Honorable Fredia S. Wadley, M.D., Commissioner
Department of Health
Cordell Hull Building, 426 Fifth Avenue North
Nashville, Tennessee 37247

Ladies and Gentlemen:

We have conducted a financial and compliance audit of selected programs and activities of the Department of Health for the year ended June 30, 2000.

We conducted our audit in accordance with generally accepted government auditing standards. These standards require that we obtain an understanding of management controls relevant to the audit and that we design the audit to provide reasonable assurance of the Department of Health's compliance with the provisions of laws, regulations, contracts, and grants significant to the audit. Management of the Department of Health is responsible for establishing and maintaining internal control and for complying with applicable laws and regulations.

Our audit disclosed certain findings which are detailed in the Objectives, Methodologies, and Conclusions section of this report. The department's administration has responded to the audit findings; we have included the responses following each finding. We will follow up the audit to examine the application of the procedures instituted because of the audit findings.

We have reported other less significant matters involving the department's internal control and instances of noncompliance to the Department of Health's management in a separate letter.

Sincerely,

John G. Morgan
Comptroller of the Treasury

JGM/ms
00/091

State of Tennessee

Audit Highlights

Comptroller of the Treasury

Division of State Audit

Financial and Compliance Audit
Department of Health
For the Year Ended June 30, 2000

AUDIT SCOPE

We have audited the Department of Health for the period July 1, 1999, through June 30, 2000. Our audit scope included those areas material to the Tennessee Comprehensive Annual Financial Report for the year ended June 30, 2000, and the Tennessee Single Audit Report for the same period. These areas included the Special Supplemental Nutrition Program for Women, Infants, and Children (WIC) and the Block Grant for Prevention and Treatment of Substance Abuse (SAPT). In addition to those areas, our primary focus was on management's controls and compliance with policies, procedures, laws, and regulations in the areas of contracts, contingent and deferred revenue, Patient Tracking and Billing Management Information System, payroll and personnel, the utilization of the Department of Finance and Administration's State of Tennessee Accounting and Reporting System (STARS) grants module to record the receipt and expenditure of federal funds, cost allocation plans for subrecipients, and cash receipting procedures. The audit was conducted in accordance with generally accepted government auditing standards.

AUDIT FINDINGS

Incorrect Grant-Funding Information in the State's Property System*

The department did not record correct grant information for equipment items that were federally funded (page 12).

No Procedures to Detect Dual Participation in the WIC and CSFP Programs*

The department has no procedures to ensure that dual participation between the Special Supplemental Nutrition Program for Women, Infants, and Children (WIC) and the Commodity Supplemental Food Program (CSFP) will be detected (page 13).

Subrecipients' Audit Reports Not Adequately Monitored**

As noted in the eight prior audits, the subrecipients' audit reports were not received timely; the reports did not contain the required schedules; and audit exceptions noted in the reports were not followed up or resolved timely (page 14).

Improper Employer-Employee Relationships**

The department has established improper employer-employee relationships through contracts with community services agencies,

human resource agencies, and other nonprofit organizations (page 16).

Inadequate Contract Controls**

The department did not approve contracts before the beginning of the contract period (page 19).

Quarterly Expenditure Reports Not Monitored

The department did not ensure that subrecipients' quarterly expenditure reports were adequately monitored (page 20).

Subrecipients' Cost Allocation Plans Not Reviewed

The department did not review subrecipients' cost allocation plans (page 25).

No Reconciliation Process to Ensure Funds Received Are Deposited

The South Central Regional Office does not reconcile cash receipts with bank deposits (page 26).

* This finding is repeated from the prior audit.

** This finding is repeated from prior audits.

"Audit Highlights" is a summary of the audit report. To obtain the complete audit report which contains all findings, recommendations, and management comments, please contact

Comptroller of the Treasury, Division of State Audit
1500 James K. Polk Building, Nashville, TN 37243-0264
(615) 741-3697

Financial/compliance audits of state departments and agencies are available on-line at
www.comptroller.state.tn.us/sa/reports/index.html.

For more information about the Comptroller of the Treasury, please visit our Web site at www.comptroller.state.tn.us.

Audit Report
Department of Health
For the Year Ended June 30, 2000

TABLE OF CONTENTS

	<u>Page</u>
INTRODUCTION	1
Post-Audit Authority	1
Background	1
AUDIT SCOPE	2
PRIOR AUDIT FINDINGS	2
Resolved Audit Finding	2
Repeated Audit Findings	3
OBJECTIVES, METHODOLOGIES, AND CONCLUSIONS	3
Areas Related to Tennessee's Comprehensive Annual Financial Report and Single Audit Report	3
Special Supplemental Nutrition Program for Women, Infants, and Children (WIC) and Block Grant for Prevention and Treatment of Substance Abuse (SAPT)	4
Finding 1 The department did not record correct grant-funding information in the state's property records	12
Finding 2 The Department of Health has no procedures to detect dual participation in the WIC and CSFP programs	13
Finding 3 Monitoring of subrecipients' audit reports is not adequate	14
Contracts	16
Finding 4 For the past 15 years, the department has continued to establish improper employer-employee relationships	16
Finding 5 The department did not approve contracts before the beginning of the contract period	19

	<u>Page</u>
Finding 6 The department did not adequately monitor quarterly expenditure reports from subrecipients	20
Contingent and Deferred Revenue	21
Patient Tracking and Billing Management Information System	22
Payroll and Personnel	23
Department of Finance and Administration Policy 20, “Recording of Federal Grant Expenditures and Revenues”	23
Department of Finance and Administration Policy 03, “Uniform Reporting Requirements and Cost Allocation Plans for Subrecipients of Federal and State Grant Monies”	24
Finding 7 Subrecipients’ cost allocation plans were not properly reviewed	25
Cash Receipting Procedures – South Central Regional Office	26
Finding 8 The South Central Regional Office does not have a reconciliation process to ensure that funds received are deposited, and resulting losses were not promptly reported	26
OBSERVATIONS AND COMMENTS	28
Title VI of the Civil Rights Act of 1964	28
TennCare Eligibility – Bradley County Health Department	28
APPENDIX	29
Divisions and Allotment Codes	29
General Fund Expenditures	30
Expenditures by Allotment and Division	30
Funding Sources	30

Department of Health For the Year Ended June 30, 2000

INTRODUCTION

POST-AUDIT AUTHORITY

This is the report on the financial and compliance audit of the Department of Health. The audit was conducted pursuant to Section 4-3-304, *Tennessee Code Annotated*, which authorizes the Department of Audit to “perform currently a post-audit of all accounts and other financial records of the state government, and of any department, institution, office, or agency thereof in accordance with generally accepted auditing standards and in accordance with such procedures as may be established by the comptroller.”

Section 8-4-109, *Tennessee Code Annotated*, authorizes the Comptroller of the Treasury to audit any books and records of any governmental entity that handles public funds when the Comptroller considers an audit to be necessary or appropriate.

BACKGROUND

The mission of the Department of Health is to promote, protect, and restore the health of Tennesseans by facilitating access to high quality preventive and primary care services. To fulfill this mission, the department comprises seven functional sections: Executive Administration; Office of Budget and Finance; Bureau of Information Systems; Office of Health Licensure and Regulations; Bureau of Alcohol and Drug Abuse Services; Bureau of Health Services; and Policy Planning and Assurance.

One of the department’s many responsibilities is to provide overall direction to, coordination of, and supervision for the state and local health departments to enable them to meet the health needs of the state’s citizens. The department ensures the quality of medical resources available in the state through the regulation, certification, and licensure of health professionals and health care facilities. The central office works in coordination with eight rural and six metropolitan regional offices and 95 county health departments to provide services, which protect and promote health and prevent disease and injury. The department also works to improve access to quality health care services in underserved areas of the state and to underserved populations. To decrease the incidence and prevalence of alcohol and other drug abuse and dependence, the department coordinates prevention, treatment, and rehabilitation services. The department is also responsible for preserving and issuing copies of all vital records.

Executive Order 24 was issued on October 19, 1999, to transfer the TennCare program and its related functions and administrative support from the Department of Health to the Department of Finance and Administration.

AUDIT SCOPE

We have audited the Department of Health for the period July 1, 1999, through June 30, 2000. Our audit scope included those areas material to the Tennessee Comprehensive Annual Financial Report for the year ended June 30, 2000, and to the Tennessee Single Audit Report for the same period. These areas include the Special Supplemental Nutrition Program for Women, Infants, and Children (WIC) and the Block Grant for Prevention and Treatment of Substance Abuse (SAPT). In addition to those areas, our primary focus was on management's controls and compliance with policies, procedures, laws, and regulations in the areas of contracts, contingent and deferred revenue, Patient Tracking and Billing Management Information System, payroll and personnel, the utilization of the Department of Finance and Administration's State of Tennessee Accounting and Reporting System (STARS) grants module to record the receipt and expenditure of federal funds, cost allocation plans for subrecipients, and cash receipting procedures. The audit was conducted in accordance with generally accepted government auditing standards.

PRIOR AUDIT FINDINGS

Section 8-4-109, *Tennessee Code Annotated*, requires that each state department, agency, or institution report to the Comptroller of the Treasury the action taken to implement the recommendations in the prior audit report. The Department of Health filed its report with the Department of Audit on December 20, 2000. A follow-up of all prior audit findings was conducted as part of the current audit. The follow-up of the year ended June 30, 1999, audit findings 1 through 31 concerning the Medical Assistance Program (Medicaid/TennCare) was conducted and reported as a part of the audit of the Department of Finance and Administration for the year ended June 30, 2000.

RESOLVED AUDIT FINDING

The current audit disclosed that the Department of Health has corrected the previous audit finding concerning accounting for Block Grant for Prevention and Treatment of Substance Abuse (SAPT) expenditures.

REPEATED AUDIT FINDINGS

The prior audit report also contained findings concerning

- recording of grant information in property records;
- detection of dual participation between the Special Supplemental Nutrition Program for Women, Infants, and Children (WIC) and the Commodity Supplemental Food Program (CSFP);
- monitoring of subrecipients' audit reports; and
- untimely approval of contracts.

These findings have not been resolved and are repeated in the Objectives, Methodologies, and Conclusions section of this report.

Another finding regarding improper employer-employee relationships was mistakenly reported as resolved in the prior audit report. That finding is again reported in the Contract area of the Objectives, Methodologies, and Conclusions section of this report.

OBJECTIVES, METHODOLOGIES, AND CONCLUSIONS

AREAS RELATED TO TENNESSEE'S COMPREHENSIVE ANNUAL FINANCIAL REPORT AND SINGLE AUDIT REPORT

Our audit of the Department of Health is an integral part of our annual audit of the Comprehensive Annual Financial Report (CAFR). The objective of the audit of the CAFR is to render an opinion on the State of Tennessee's general-purpose financial statements. As part of our audit of the CAFR, we are required to gain an understanding of the state's internal control and determine whether the state complied with laws and regulations that have a material effect on the state's general-purpose financial statements.

Our audit of the Department of Health is also an integral part of the Tennessee Single Audit which is conducted in accordance with the Single Audit Act, as amended by the Single Audit Act Amendments of 1996. The Single Audit Act, as amended, requires us to determine whether

- the state complied with rules and regulations that may have a material effect on each major federal financial assistance program, and
- the state has internal control to provide reasonable assurance that it is managing its major federal programs in compliance with applicable laws and regulations.

We determined the following areas within the Department of Health were material to the CAFR and to the Single Audit Report: the Special Supplemental Nutrition Program for Women, Infants, and Children (WIC) and the Block Grant for Prevention and Treatment of Substance Abuse (SAPT).

To address the objectives of the audit of the CAFR and the Single Audit Report, as they pertain to these two major federal award programs, we interviewed key department employees, reviewed applicable policies and procedures, and tested representative samples of transactions. For further discussion, see the applicable sections (WIC and SAPT).

We have audited the general-purpose financial statements of the State of Tennessee for the year ended June 30, 2000, and have issued our report thereon dated November 29, 2000. The opinion on the financial statements is unqualified. The Tennessee Single Audit Report for the year ended June 30, 2000, includes our reports on the schedule of expenditures of federal awards and on internal control and compliance with laws and regulations. These reports include reportable conditions and material weaknesses resulting from this audit. These reports also include instances of noncompliance resulting from this audit.

The audit of the department revealed the following findings in areas related to the CAFR and the Single Audit Report:

- The department did not record correct grant-funding information in the state's property records. See finding 1.
- The department had no procedures to detect dual participation in the WIC and Commodity Supplemental Food Program. See finding 2.
- Monitoring of subrecipients' audit reports is not adequate. See finding 3.

SPECIAL SUPPLEMENTAL NUTRITION PROGRAM FOR WOMEN, INFANTS, AND CHILDREN (WIC) AND BLOCK GRANT FOR PREVENTION AND TREATMENT OF SUBSTANCE ABUSE (SAPT)

The two major federal programs for the Department of Health were audited for the applicable compliance requirements as noted in the U.S. Office of Management and Budget Circular A-133, *Compliance Supplement for Audits of States, Local Governments, and Non-Profit Organizations*. These two major programs are Special Supplemental Nutrition Program for Women, Infants, and Children (WIC) and Block Grant for Prevention and Treatment of Substance Abuse (SAPT).

To address the objectives of the CAFR and the Single Audit, as they pertain to federal financial assistance programs, our audit focused primarily on the compliance requirements for WIC and SAPT.

The audit consisted of the following areas:

- Activities Allowed or Unallowed and Allowable Costs / Cost Principles
- Cash Management
- Eligibility
- Equipment and Real Property Management
- Matching, Level of Effort, Earmarking
- Period of Availability of Federal Funds
- Procurement and Suspension and Debarment
- Program Income
- Reporting
- Subrecipient Monitoring
- Special Tests and Provisions
- Schedule of Expenditures of Federal Awards

Activities Allowed or Unallowed and Allowable Costs / Cost Principles

The primary objectives for both WIC and SAPT were to determine if

- funds were used for allowable purposes, and
- expenditures involving federal funds have been recorded correctly as to the proper grant program and applicable federal grant.

An additional objective for WIC was to determine if costs meet the criteria set forth in the “Basic Guidelines” of OMB Circular A-87, *Cost Principles for State, Local and Indian Tribal Governments*, Attachment A, paragraph C.

Supporting documentation for all WIC and SAPT significant items and a nonstatistical sample of SAPT expenditures were reviewed and tested to determine if funds were used for allowable purposes and appropriately recorded to the proper grant program and applicable federal grant. Also, where applicable, the items were tested for compliance with travel regulations, contract terms, and purchasing guidelines. Supporting documentation for all WIC significant items was reviewed and tested to determine if costs were in compliance with OMB Circular A-87.

Our testwork indicated that the department’s federal WIC and SAPT funds appeared to be used for allowable activities, and expenditures appeared to be recorded correctly as to the proper grant program and the applicable federal grant. WIC costs appeared to be in compliance with OMB Circular A-87.

Cash Management

The primary objectives for WIC and SAPT were to determine if

- the department complied with the Cash Management Improvement Act Agreement between the State of Tennessee and the Secretary of the Treasury, United States Department of the Treasury; and
- the department's reporting of receipt and disbursement transactions to the Department of Finance and Administration was adequate.

For both WIC and SAPT, the department's policies and procedures for recording and reporting the costs and drawdowns to the Department of Finance and Administration were reviewed and discussed with the appropriate personnel. We selected a nonstatistical sample of drawdown transactions and compared the process dates of the expenditure transactions in the State of Tennessee Accounting and Reporting System (STARS) with the dates the funds were requested from the federal agency to determine if drawdown requests were in compliance with the Cash Management Improvement Act.

Our testwork indicated that the department complied with the Cash Management Improvement Act Agreement between the State of Tennessee and the Secretary of the Treasury, United States Department of the Treasury. Also, the department's reporting of receipt and disbursement transactions to the Department of Finance and Administration was adequate.

Eligibility

The primary objective for WIC was to determine if the department makes the required eligibility determinations (including obtaining any required documentation/verifications), and that individual program participants were deemed to be eligible and only eligible individuals or groups of individuals participated in the program.

A nonstatistical sample of WIC participants was selected. We accessed the Patient Tracking and Billing Management Information System and reviewed each selected participant's records for the appropriate information to determine if the department made an appropriate determination as to whether the participant was income eligible, met the residency requirement, was given the correct status or category, and was certified for nutritional risk by a qualified nutritionist.

Our testwork indicated that the department performed the required eligibility determinations and only eligible individuals or groups of individuals participated in the program.

Equipment and Real Property Management

The primary objectives for WIC and SAPT were

- to follow up on the prior audit finding concerning the recording of grant information in property records,
- to determine if equipment items existed and were recorded on the property listing at the proper cost,
- to determine if equipment purchases charged to federal grants were in compliance with grant requirements, and
- to determine if disposition or encumbrance of any equipment acquired under federal awards was in accordance with federal requirements and that the awarding agency was compensated for its share of any equipment sold or converted to non-federal use.

A nonstatistical sample of WIC and SAPT equipment expenditures charged to the major federal programs was selected to determine if the equipment items existed and were recorded on the property listing at the proper cost. Supporting documentation was reviewed and the information was traced to the Property of the State of Tennessee listing (POST) and STARS to determine if equipment items purchased with federal funds were identified on the property system with the correct grant information and whether the purchase complied with the applicable federal regulations. Also, supporting documentation of surplus equipment was reviewed to determine if disposition of federally funded equipment was in accordance with federal requirements.

Based on our testwork, the equipment items sampled existed, were recorded on the property listing at proper cost, and were purchased in compliance with grant requirements. However, not all federally funded equipment was recorded on the property listing with the proper federal funding source. Therefore, identification of federally funded surplus equipment and compliance with federal requirements could not be determined. This deficiency, which is disclosed in repeat finding 1, was department-wide and involved all federal programs.

Matching, Level of Effort, Earmarking

The primary objectives for SAPT were

- to follow up on the prior audit finding concerning the accounting for SAPT expenditures, and
- to determine if the department met the required level of effort and earmarking.

Matching is not a requirement of OMB Circular A-133 for the SAPT block grant.

OMB Circular A-133, *Compliance Supplement for Audits of States, Local Governments, and Non-Profit Organizations*, and other program guidelines were reviewed to become familiar with program objectives, procedures, and major compliance requirements. The amount of non-

federal funds expended for the year ending June 30, 2000, and the average level of expenditures maintained for the preceding two-year period were obtained and reviewed to determine if the department maintained state expenditures for authorized activities in accordance with the level of effort requirements.

The state must maintain grant expenditures for Substance Abuse (SA) treatment services for pregnant women and women with dependent children in accordance with the level of effort requirements. Also the state must maintain expenditures of non-federal amounts for HIV and tuberculosis services in accordance with the level of effort requirements. The expenditures were traced to supporting documentation.

Required percentages of the block grant funds are to be expended for prevention and treatment activities regarding alcohol, for prevention and treatment of other drugs, for one or more projects to make available to individuals early intervention services for HIV disease at the sites where the individuals are undergoing SA treatment, and for the costs of administering the grant. The amounts of block grant funds were traced to STARS to determine if the required percentages were met.

Based on our testwork, the department met the required level of effort and earmarking.

Period of Availability of Federal Funds

The primary objective for both WIC and SAPT was to determine if the department obligated federal funds within the period of availability and obligations were liquidated within the required time period.

Financial reports, contracts, and expenditures were reviewed and traced to supporting documentation to determine if funds were obligated and expended within periods allowed.

Based on our review of financial reports, contracts, and expenditures, the department obligated federal funds within the period of availability and obligations were liquidated within the required time period.

Procurement and Suspension and Debarment

The primary objectives for WIC and SAPT were to determine if

- procurement of goods and services was made in compliance with the provisions of applicable regulations and guidelines, and
- any subaward, contract, or agreement for purchase of goods or services was made with any debarred or suspended party.

For both WIC and SAPT, the department's purchases of equipment and supplies were handled through the Tennessee On-line Purchasing System (TOPS). We selected a nonstatistical sample of purchases from TOPS to test for compliance with requirements contained in OMB

Circular A-133, *Compliance Supplement for Audits of States, Local Governments, and Non-Profit Organizations*. In addition, all WIC and a nonstatistical sample of SAPT contracts were obtained and reviewed for the clause stating that the contractor had not been suspended or debarred and for the appropriate signature.

Based on our testwork, it appeared that management had complied with procurement requirements, and that no subaward, contract, or agreement for purchase of goods or services was made with any debarred or suspended party.

Program Income

The primary objective for WIC was to determine if program income was correctly recorded and used in accordance with the program requirements.

The program income, which is the interest received on infant formula rebates, was traced to supporting documentation to determine if the program income components were properly identified and had been used for allowable purposes.

Based on our testwork, program income was correctly recorded and used in accordance with the program requirements.

Reporting

The primary objective for both WIC and SAPT was to determine if the required reports for federal awards included all activity of the reporting period, were supported by applicable accounting or performance records, and were presented in accordance with program requirements. An additional objective for WIC was to follow up on the prior audit finding concerning detection of dual participation between WIC and the Commodity Supplemental Food Program (CSFP).

The required financial reports for WIC federal awards were reviewed for completeness and timeliness of submission. Key line items on the *WIC Monthly Financial Management and Participation Report* and *WIC Program Annual Closeout Report* were traced to documentation to determine if the reports were adequately supported and presented in accordance with program requirements. The required monthly CSFP and WIC dual participation reports were requested to determine if the department was producing and reviewing the reports timely.

For SAPT, the key line items on the *Summary of Tobacco Results by State Geographic Sampling Unit* were traced to adequate supporting documentation provided by the Tennessee Department of Agriculture to determine if the department was performing the required inspections of establishments that sell tobacco products.

Based on our reviews and testwork, it appears that the required reports for federal awards included all activity of the reporting period, were supported by applicable accounting or performance records, and were presented in accordance with program requirements. However,

the department did not produce the monthly CSFP and WIC reports to detect dual participation as disclosed in finding 2.

Subrecipient Monitoring

The primary objectives for both WIC and SAPT were

- to follow up on the prior audit finding concerning monitoring of subrecipients' audit reports;
- to determine whether the department was in compliance with the Department of Finance and Administration's Policy 22 concerning subrecipient monitoring;
- to determine if the department monitored subrecipient activities to provide reasonable assurance that the subrecipients administer federal awards in compliance with federal requirements;
- to determine whether program subrecipients were monitored for compliance with program guidelines; and
- to determine if the department's procedures for obtaining and reviewing subrecipients' audit reports to identify and resolve subrecipient weaknesses in internal control, instances of noncompliance with subrecipient agreements, and questioned costs were functioning in accordance with prescribed requirements.

The department's procedures for monitoring local agencies' eligibility and activity, for monitoring program subrecipients at both program and fiscal levels, and for evaluating authorized vendors were reviewed and evaluated for adequacy. The department's procedures for evaluating subrecipients to be monitored, developing a monitoring plan, and submission of the monitoring plan and annual report were reviewed and evaluated to determine compliance with the Department of Finance and Administration's Policy 22. A nonstatistical sample of monitoring reports was reviewed to determine if the special requirements, as described in the program guidelines and regulations, were included in the monitoring report. The department's procedures were reviewed to determine if the department obtained and evaluated subrecipients' audit reports timely. We also tested a nonstatistical sample of audit reports to determine if monitoring results were documented and whether deficiencies were corrected appropriately and timely.

Based on our review and testwork, the department's program and fiscal monitoring of subrecipient activities to provide reasonable assurance that the subrecipient administers federal awards in compliance with federal requirements was adequate. Also, the department complied with Department of Finance and Administration's Policy 22, and the department's monitoring of program subrecipients for compliance with program guidelines was adequate. However, the department's procedures for obtaining and reviewing subrecipients' audit reports for the purpose of identifying and resolving subrecipient weaknesses in internal control, instances of noncompliance with subrecipient agreements, and questioned costs were not adequate. See finding 3.

Special Tests and Provisions

One-to-One Reconciliation

For WIC, the primary objective was to determine whether the department's food instruments reconciliation process complied with the one-to-one reconciliation requirement.

Reconciliation reports of redeemed food instruments and exception listings were reviewed to determine that the department's non-reconciliation rate did not exceed one percent. We reviewed the department's controls over the bank's contract with WIC to determine if food instruments were redeemed in compliance with the federal requirements.

Based on our reviews and testwork, the department's reconciliation process of food instruments complied with the one-to-one reconciliation requirement.

Management Evaluations

For WIC, the primary objectives were to determine whether the department has conducted the required local agency management reviews and that the local agency management reviews cover the required areas.

The Summary of Clinic Reviews and Clinic Listings were obtained and all reviewed regions were tested to determine if the department conducted the required local agency management reviews, including a minimum of 20% of on-site visits of the clinics in the region. Also, the sample was tested to determine if the local agency management reviews covered the required areas.

Our review and testwork indicated that the reviews covered the required areas, and the department complied with the 20% monitoring requirement.

Independent Peer Reviews

For SAPT, the primary objectives were to determine whether (1) the required number of entities were peer reviewed, (2) the selection of entities for peer review was representative of entities providing services, (3) and the state ensured that the peer reviewers were independent.

We obtained and reviewed the listing of agencies providing treatment programs and the listing of agencies receiving peer reviews to determine if the number of entities reviewed was in compliance with the federal requirements. Also, a nonstatistical sample was tested to determine if the selected entities for peer review were representative of entities providing service and that the department ensured that the peer reviewers were independent.

Based on our reviews and testwork, the required number of entities were peer reviewed, the selection of entities was representative of entities providing services, and the department ensured the peer reviewers were independent.

Schedule of Expenditures of Federal Awards

Our objective was to verify that the Schedule of Expenditures of Federal Awards was properly prepared and adequately supported. We verified the grant identification information on the Schedule of Expenditures of Federal Awards, and total disbursement amounts were traced to supporting documentation. Based on the testwork performed, we determined that the Schedule of Expenditures of Federal Awards appeared to be properly prepared and adequately supported.

Findings, Recommendations, and Management's Comments

1. The department did not record correct grant-funding information in the state's property records

Finding

As noted in the previous audit, the Department of Health did not record correct grant-funding information in the state's property records. Management concurred with the prior finding and stated that the department's policy of recording correct grant-funding information on the purchase request for all equipment would be reinforced.

However, testwork revealed that the department still does not always record the grant number and percentage of federal funds into Property of the State of Tennessee (POST), the state's property and equipment tracking system, for some equipment items purchased with federal funds. Five of 22 federally funded equipment items (23%) were incorrectly listed as state funded in POST. Of the five equipment items, three were purchased with federal Special Supplemental Nutrition Program for Women, Infants, and Children (WIC) funds and two were purchased with federal Block Grant for Prevention and Treatment of Substance Abuse (SAPT) funds. Incorrect funding information resulted because requesting employees did not follow the department's policy of recording accurate information on the purchase request and there was not a reconciliation of federally funded equipment purchases from the accounting system to the property records.

The department must be able to distinguish between state and federal property. According to the *Code of Federal Regulations* for WIC at Title 7, Part 3016, Section 32 (d)(1), and for SAPT at Title 45, Part 92, Section 32(d)(1), the property records have to include the "percentage of Federal participation in the cost of the property," regardless of the price. If the equipment is damaged beyond repair, lost, or stolen, the recipient may be accountable to the awarding agency of the federal government for a calculated amount of the federal participation of the original purchase price times the fair market value. If equipment purchased with federal funds is not correctly identified in the property records, the department's ability to transfer equipment, dispose of equipment, or reimburse the federal government in accordance with federal laws and regulations is greatly diminished.

Recommendation

Employees who initiate equipment purchases that are to be funded with federal funds should include correct grant information on the face of the purchase documents. Supervisors should verify that all funding information is complete and correct prior to approving the purchase documents. Also, the Information System Analyst in Fiscal Services should provide a listing of all federally funded equipment purchases based on information from the State of Tennessee Accounting and Reporting System (STARS) to the Property Officer. The Property Officer should then reconcile POST to the listing to ensure that the appropriate grant information is recorded in the property system. This reconciliation should be done at least annually. The Director of the Division of General Services should ensure that this reconciliation is performed.

Management's Comment

We concur and have changed our internal process. The Division of Fiscal Services furnishes the Division of Central Procurement and Payments a quarterly listing of equipment purchases utilizing federal funds. This list gives the correct grant information which is reconciled to POST by the Property Officer. The Property Officer changes any incorrect grant information in POST, and returns the list to the Division of Fiscal Services.

2. The Department of Health has no procedures to detect dual participation in the WIC and CSFP programs

Finding

As noted in the prior audit, the Department of Health does not have adequate controls to ensure that dual participation between the Special Supplemental Nutrition Program for Women, Infants, and Children (WIC) and the Commodity Supplemental Food Program (CSFP) will be detected. In response to the prior finding, management stated that all four local agencies would be connected to the Patient Tracking and Billing Management Information System (PTBMIS) by July 2000. As of November 3, 2000, one of the four local agencies was still not connected to PTBMIS. In fact, this one local agency is still keeping track of the participants it is serving manually. Management's prior response also stated that by March 2000 the Central Office would be able to compare WIC and CSFP populations to detect dual participation between local agencies. From February of 1998 through July of 2000, no dual participation reports between local agencies had been generated. The populations compared in August of 2000 did not include the participants of the one local agency mentioned above because the participant information is maintained manually. Because the one local agency is not connected to PTBMIS and the dual participation reports are not generated each month, participants may improperly receive benefits from both WIC and CSFP programs.

According to the *Code of Federal Regulations*, Title 7, Part 246, Section 7(l)(1)(i), the state agency “shall be responsible for . . . the prevention and detection of dual participation within each local agency and between local agencies.”

Recommendation

The Director of the Bureau of Information Resources and the Supplemental Nutrition Program Director should ensure that the one local agency without access to PTBMIS obtains access and that the dual participation reports are generated. They should also monitor operations to ensure that the corrective action is taken when problems occur.

Management’s Comment

We concur. The Telecommunications Department of Memphis/Shelby County is awaiting a quote for the frame relay and cabling necessary to connect MAP South to PTBMIS. Once received, the installation should take no longer than two weeks to complete. Staff will then install the computer equipment to complete the connection to our PTBMIS and we anticipate MAP South will be fully connected by February 28, 2001. This will allow the Department to identify any dual participation in the WIC and CSFP program.

3. Monitoring of subrecipients’ audit reports is not adequate

Finding

As noted in the eight prior audits, the Department of Health does not adequately monitor subrecipients’ audit reports. Management concurred with the prior findings and stated the department would more aggressively pursue the receipt of the audit reports within the required time frames, attempt to ensure that all required supporting documentation is provided, put more emphasis on reviewing questioned and disallowed costs, and issue timely management decisions.

Testwork on 29 subrecipients’ audit reports received in the audit period that were subject to the Office of Management and Budget Circular A-133 reporting standards revealed the following deficiencies:

- Twenty-six audit reports (90%) were not received within the nine-month deadline. The reports were received 12 to 471 days late, or an average of 200 days late. Thirteen of the audit reports were due on March 31, 2000; 11 audit reports were due on March 31, 1999; and 2 audit reports were due on September 30, 1999.
- One audit report (3%) did not have the required Schedule of Findings and Questioned Costs. Only after the auditors informed the department about the missing schedule did the department obtain the schedule.

- Only one audit report contained findings, and no evidence could be provided that a management decision had been issued regarding the findings. A management decision is the evaluation by the awarding agency of the subrecipient's audit findings and corrective action plan and the issuance of a written decision as to what corrective action is necessary.
- No actions were taken against subrecipients for not obtaining timely audits in accordance with OMB Circular A-133.

OMB Circular A-133 states that the audit report should be submitted within nine months after the end of the audit period. It also states that "the auditor's report(s) shall . . . include . . . a schedule of findings and questioned costs." The three required components of the schedule are a summary of auditor's results, findings related to the financial statements, and findings and questioned costs for federal awards.

The circular also states that it is the pass-through entity's (Department of Health's) responsibility to "issue a management decision on audit findings within six months of receipt of the subrecipient's audit report." The circular requires that the management decision "shall clearly state whether or not the audit finding is sustained, the reasons for the decision, . . . any appeal process," and the audit finding reference numbers. The management decision shall also include "the expected auditee action to repay disallowed costs." Furthermore, it states that "in cases of continued inability or unwillingness to have an audit conducted in accordance with this part, . . . pass-through entities shall take appropriate action using sanctions such as . . . withholding a percentage of Federal awards until the audit is completed satisfactorily" or "suspending Federal awards until the audit is conducted."

Recommendation

The department should ensure that subrecipients' required audit reports are received no later than nine months following their fiscal year end, the reports are reviewed for completeness, and the management decisions on audit findings are issued, as required by OMB Circular A-133. The Office of Audit and Investigations should develop a checklist of the required information for this type of audit report. The checklist could also be used to document the review of the audit report. The Commissioner should take appropriate action using such sanctions as withholding a percentage of funding from any subrecipient when the required audit is not conducted or the audit report is not submitted to the department timely.

Management's Comment

We concur. Additional personnel have been devoted to the monitoring of subrecipient audits. The Department has also begun sending written notification to subrecipients for their audits 3 months before the 9-month deadline required by OMB A-133. We will develop a checklist of required information for audits of subrecipients and will obtain the Schedule of Findings and Questioned Costs when audits lack this schedule. Further, timely management decisions on audit findings will be issued. In addition, consideration will be given to imposing

the sanctions suggested by OMB Circular A-133 in cases of continued inability or unwillingness of a subrecipient to have an audit conducted in accordance with the Circular. However, it should be noted, the only instance where subrecipients failed to provide us with their audit was when the subrecipient organization became defunct.

Lastly, the Department is writing a policies and procedures manual for monitoring audits of subrecipients.

CONTRACTS

Our primary objective in the area of contracts was to follow up on the prior audit finding concerning the untimely approval of contracts, and our additional specific objectives were to determine

- whether the department continued to enter into contracts that establish improper employer-employee relationships,
- whether the department allowed contract services to be rendered before proper approvals of the contracts were obtained, and
- whether the department had adequately monitored subrecipients' quarterly expenditure reports.

We interviewed key department personnel and reviewed terms of contracts, authorizations and dates, contract payment support, memorandums, and expenditure reports.

Based on our testwork, the department had entered into contracts that established improper employer-employee relationships (see finding 4), allowed contract services to be rendered before proper approvals of the contracts were obtained (see finding 5), and did not adequately monitor quarterly expenditure reports (see finding 6).

Findings, Recommendations, and Management's Comments

4. For the past 15 years, the department has continued to establish improper employer-employee relationships

Finding

As noted in audit reports since 1986, the Department of Health has entered into contracts with a nonprofit organization, community service agencies, and human resource agencies to assist in implementing different programs. Through these contracts, the department has directed these organizations and agencies to provide individuals who are directly supervised by state officials. In spite of contract language designed to prohibit an employer-employee relationship between the department and contracting agencies, these contracts apparently create "employer-

employee” relationships between the department and these individuals employed by the contractors. Management concurred with the prior findings and has been reducing the number of these relationships through attrition or hiring the employee as a state or county employee, as the positions become available. Due to management reducing the number of such relationships, we understood that this situation was being resolved and reported accordingly in the fiscal year ended June 30, 1999, audit report. However, during current audit testwork, it was revealed that the department still has approximately 107 such relationships.

The practice of allowing employees of non-state entities to report directly to department officials/employees in carrying out what can be construed as state programs raises policy and legal issues. We do not believe that these situations should be accepted as a matter of policy. Chapter 0620-3-3-.03(b) of the *Rules of the Department of Finance and Administration* states that contracts representing the hiring of employees are improper. It continues to state that employees should be hired through the Department of Personnel, according to state policy. These rules further provide factors to consider when determining whether a contract is representing the hiring of employees. Such factors include the following:

- to what extent civil servants could do the work, and whether the contractor has specialized knowledge or equipment unavailable to the state (titles of positions and the related job specifications for the workers are taken directly from the State of Tennessee Department of Personnel);
- to what extent the services represent the discharge of a state function calling for the exercise of personal discretion on behalf of the state (the state retains the basic responsibility for the administration of the program and prescribes using the state’s WIC voucher system for the distribution of supplemental food);
- the extent to which the need is continuing rather than short-term or intermittent (some of these agreements have been in place with the same agencies for 15 years);
- the extent to which the state has control over qualifications of the employees of the contractor (titles of positions and the related job specifications for the workers required under the contracts are taken directly from the State of Tennessee Department of Personnel);
- the extent to which the state has the right to assign tasks for contractor employees (contract budget summaries include names by position titles);
- whether the state has a right to review performance of contractor employees as opposed to reviewing the final product (the contract requires informing the state program office of all personnel transactions involving positions funded by the contract);
- whether the work constitutes a specific task or project as opposed to day-to-day work (the outlined tasks are day-to-day work);
- whether payment is for results accomplished as opposed to time worked (payment is based on actual costs, which include time worked); and

- whether the contractor has access to the state’s space, equipment, supplies, etc. (several of the persons work in the department’s central office using state equipment and supplies).

Also, there are other factors that are indicative of an employer-employee relationship. Such factors include the following:

- contractor employees are used interchangeably with state employees to perform the same function (state employees are also doing the same work);
- state employees provide the supervision over the contract employees;
- the work is more day-to-day and continuing in nature, as opposed to a certain project or projects, and is integrated into the department’s Patient Tracking and Billing Management Information System (PTBMIS); and
- contractor employees use the state’s space, equipment, and supplies.

In addition, the state apparently has incurred additional cost by contracting with non-state entities to provide individuals. In addition to paying the salaries and benefits, travel, training, and supplies of these “employees,” an additional administrative fee is paid to these organizations.

Recommendation

The Department of Health should not contract with nonprofit organizations, community service agencies, and human resource agencies to provide individuals who are, in effect, performing state services and should be placed on the state payroll system through the proper hiring procedures. When appropriate, the department should establish either professional service or personal service contracts. However, such contracts should clearly be used for hiring an independent contractor and should not establish an employer-employee relationship.

Management’s Comment

We do not concur. Our contractual relationship is with an independent contractor and not with any of their individual employees. The Department does not have any authority over the hiring or disciplinary decisions for any of the contract employees other than removal for misconduct or security reasons. Management does acknowledge the contracts are specific in the position descriptions required and exercises oversight in performance of the grantee’s activities. This is viewed as no more than a routine monitoring function to ensure programmatic and fiscal activities are being performed in compliance with the contract’s scope of services.

In regards to the payments being based on cost, this is a routine payment methodology utilized in our contracts and throughout the State. Further, a contract budget summary with names reflected by position title represents nothing more than a budget for determining legitimate cost and the maximum financial liability for the contractor’s performance of the

contract's scope of services. Lastly, the State has always had discretion in contract negotiations in regards to a grantee's access to State equipment, space, and other resources in performance of the grant's scope of services.

However, in an effort to eliminate concerns regarding this situation, the Department will continue to assess our contractual arrangements. As we identify functions and activities which should be under direct supervision of departmental staff and state positions become available, contractual arrangements will be modified or terminated to reflect only those contractual services required.

Rebuttal

The employer-employee guidelines covered in the Department of Finance and Administration's rules state that these factors will be used to determine if this type of relationship exists. When these mentioned factors are examined collectively, they indicate that this type of relationship exists between the Department of Health and the contractor's employees, even though the grant contract is between the Department of Health and the contractors. Management even states in its comment that contracts will be modified or terminated, when deemed appropriate. These relationships raise policy and legal issues for the department.

5. The department did not approve contracts before the beginning of the contract period

Finding

As noted in the two prior audits, the Department of Health did not approve contracts before the beginning of the contract period. Management concurred with the prior two findings and stated that timeliness in submitting the contracts for approval would be stressed at the program and vendor level.

However, testwork revealed that the department still does not always approve contracts before the beginning of the contract period. Thirty-eight of 75 contracts (50.7%) with a beginning date of July 1, 2000, were approved an average of 43 days late. As of November 20, 2000, one additional contract was still not fully approved. This late approval of contracts resulted because bureau directors did not adhere to the department's internal deadline of April 1, 2000. The contracts should have been preapproved, signed by the vendor, and submitted to the Contract Office for further processing through the Department of Finance and Administration by April 1, 2000. While no payments were made against a contract until it was fully approved, potential liabilities to the state occurred because the contracts were without proper authorization.

Chapter 0620-3-3-.04(d)(8) of the *Rules of the Department of Finance and Administration* states that "upon approval by the Commissioner of Finance and Administration [the contract] shall be an effective and binding contract." If contracts are not approved before

the contract period begins and before services are rendered, the state could be obligated to pay for unauthorized services.

The department issues many of its contracts pursuant to departmental grant authorities (DGA). The DGA is sent to the Commissioner of Finance and Administration for approval. Once this approval is obtained, then the Commissioner of Health or her designee can sign the actual contracts. In order to be properly authorized, contracts pursuant to the DGA require the Commissioner's signature or that of her designee. All other contracts require the original signature of the Commissioner of the Department of Health.

Recommendation

The department's bureau directors should adhere to the department's deadlines for submitting contracts for review and Commissioner approval to help ensure the contracts will be completely approved before the beginning of the contract period.

Management's Comment

We do not concur. While some contracts are not signed before the start date indicated in the contract terms and conditions, the contract is not fully executed until all signatures are obtained. The department does not authorize payment of services before a fully executed contract is processed by the Department of Finance and Administration. The auditors have not indicated that any improper authorizations or payments have occurred. However, as a good business practice, the Department will continue to emphasize to vendors the importance of returning signed contracts to the Department in a more timely fashion.

Rebuttal

In the two prior audit reports, management concurred with this finding. In the prior audit report, management specifically stated, "We will continue to encourage procedures and stress timeliness with both the programs and vendors in order to strive toward execution of approved and signed contracts prior to their start date." However, no significant improvement was noted during the follow-up testwork on the prior finding. Management even states in its comment to this finding that it is a good business practice to have contracts fully executed before the beginning of the contract period. The failure to do so could result in the state being obligated to pay for unauthorized goods or services.

6. The department did not adequately monitor quarterly expenditure reports from subrecipients

Finding

The Department of Health did not enforce contract requirements concerning the submission of quarterly expenditure reports. Testwork on 25 contracts requiring quarterly

expenditure reports revealed that for 20 contracts the quarterly reports were not submitted or were submitted late. Some problems noted included the following:

- Cumulative final expenditure reports due August 31, 2000, for three contracts had not been submitted as of November 29, 2000.
- Cumulative final expenditure reports for eight contracts were submitted an average of 39 days late. In addition, none of the nine interim quarterly reports required by the contracts were submitted for three of these contracts. For the other five contracts, seven interim quarterly reports were submitted an average of 12 days late and three reports were not submitted.
- Thirteen interim quarterly reports were submitted an average of 88 days late, and four interim quarterly reports were not submitted for nine other contracts.

The contracts specify that the quarterly expenditure reports are to be submitted either 45 or 60 days after the end of each quarter. Private and governmental not-for-profit subrecipients are required to submit their reports within 45 days, while counties and state universities are allowed 60 days. The expenditure reports show contract expenditures categorized by object for the reported quarter and the yearly total. Therefore, the department can determine where and how the grant recipients have spent this money.

Recommendation

The Accounting Manager in Fiscal Services should monitor compliance with the contractual quarterly expenditure reporting requirements to ensure that those requirements are followed. The Commissioner should take appropriate action using such sanctions as withholding a percentage of funding from any grant recipient that demonstrates a continued unwillingness to comply with the contract reporting requirements.

Management's Comment

We concur. An Administrative Services Assistant has been hired to assist the Division of Fiscal Services and specifically the Contract Section in obtaining the quarterly expenditure reports as required.

CONTINGENT AND DEFERRED REVENUE

Our objectives were to determine whether

- contingent/deferred revenue accounts were used for the intended purpose;
- transactions were properly supported;
- only applicable items were recorded as contingent or deferred revenue and in the proper amounts;

- revenue was transferred from contingent/deferred to earned when the applicable criteria were met;
- the department had complied with applicable federal rules, regulations, and guidelines when federal funds were involved; and
- large variances between current and prior-year ending balances could be reasonably explained.

We interviewed key department personnel to gain an understanding of the department's procedures for and controls over deposits into the subaccounts and transfers to earned revenue to determine if contingent/deferred revenue accounts were used for the intended purpose. We also reviewed supporting documentation and tested nonstatistical samples of deferred revenue transactions to determine if only applicable items were recorded as contingent or deferred revenue and for the proper amount, revenue was transferred out of the subaccount when it was earned, and the department complied with applicable federal rules and regulations. We also compared June 30, 2000, subaccount balances with balances reported at June 30, 1999, and obtained explanations for significant variances.

Based on our testwork, the contingent/deferred revenue accounts were used for the intended purpose, revenue transactions were properly supported, and contingent/deferred revenue was deposited properly into and transferred out of the subaccount when the applicable criteria were met. Testwork also revealed that the department complied with applicable federal rules and regulations. Also, significant variances between current and prior-year balances were reasonably explained by department personnel.

PATIENT TRACKING AND BILLING MANAGEMENT INFORMATION SYSTEM (PTBMIS)

Our objectives for PTBMIS were to

- obtain an understanding of PTBMIS critical general and application controls,
- document the design of PTBMIS, and
- determine that the department had canceled terminated employees' access to PTBMIS.

We interviewed appropriate personnel to gain an understanding of PTBMIS. We administered the Electronic Data Processing section of the general planning and internal control questionnaire and reviewed organization charts for the Bureau of Information Resources to document the design of PTBMIS. The general control policies and procedures concerning security, system changes, and contingency planning were reviewed and assessed to gain an understanding and assess the risk of the general controls. We also reviewed the application control policies and procedures concerning audit trail, input, processing, and output to gain an understanding and assess the risk of the application control. We tested a nonstatistical sample of employee terminations to determine if access had been removed at the time of termination.

Based on our interviews and testwork, the design of PTBMIS was documented, the general and application controls were in place, and terminated employees' access to PTBMIS was canceled.

PAYROLL AND PERSONNEL

Our objectives for payroll and personnel were to determine whether

- net pay was computed accurately,
- payroll charges to grants were allowable and proper,
- the department was in compliance with the Department of Finance and Administration's Policy 11 concerning the recovery of overpayments that are owed by state employees, and
- employment could be verified.

Key department personnel were interviewed to gain an understanding of the department's procedures for and controls over payroll and personnel. We also reviewed supporting documentation and tested a nonstatistical sample of payroll transactions to determine if net pay was computed accurately, payroll charges to grants were allowable and proper, and that the individual's employment could be verified. We also followed up all employee overpayments to determine compliance with the Department of Finance and Administration's Policy 11.

Based on our testwork, net pay was computed properly, payroll charges to grants were allowable and proper, the department complied with the Department of Personnel's policies and the Department of Finance and Administration's Policy 11, and employment was verified.

DEPARTMENT OF FINANCE AND ADMINISTRATION POLICY 20, "RECORDING OF FEDERAL GRANT EXPENDITURES AND REVENUES"

Department of Finance and Administration (F&A) Policy 20 requires that state departments whose financial records are maintained on the State of Tennessee Accounting and Reporting System (STARS) fully utilize the STARS grants module to record the receipt and expenditure of all federal funds.

Our objectives were to determine whether

- appropriate grant information was entered into the STARS grant control table upon notification of the grant award, and related revenue and expenditure transactions were coded with the proper grant codes;
- appropriate payroll costs were reallocated to federal programs within 30 days of each month-end using an authorized redistribution method;

- the department made drawdowns at least weekly using the applicable STARS reports;
- the department had negotiated an appropriate indirect cost recovery plan, and indirect costs were included in drawdowns; and
- the department used the appropriate STARS reports as bases for preparing the department's schedule of expenditures of federal awards and reports submitted to the federal government.

We interviewed key personnel to gain an understanding of the department's procedures and controls concerning Policy 20 and the department's indirect cost recovery plan. We reviewed supporting documentation and tested a nonstatistical sample of drawdowns and reports submitted to the federal government to determine if indirect costs were included in the drawdowns and drawdowns were made timely. All grant award notification dates were reviewed and compared to the awards listed in STARS to determine if the grant award was entered timely. We also reviewed payroll cost reallocations and the schedule of expenditures of federal awards. Each grant's total expenditure amount on the schedule was traced to STARS.

Based on our interviews, reviews, and testwork, the department was in compliance with F&A Policy 20. The department had fully utilized the STARS grants module to record the receipt and expenditure of all federal funds, appropriate payroll costs were reallocated appropriately and timely, the department made drawdowns timely, and the proper indirect costs were included in the drawdowns. The department also used the appropriate STARS reports as bases for preparing the schedule of expenditures of federal awards and reports submitted to the federal government.

DEPARTMENT OF FINANCE AND ADMINISTRATION POLICY 03, "UNIFORM REPORTING REQUIREMENTS AND COST ALLOCATION PLANS FOR SUBRECIPIENTS OF FEDERAL AND STATE GRANT MONIES"

Department of Finance and Administration Policy 03 establishes uniform reporting requirements for certain subrecipients and requires those subrecipients' cost allocation plans to be reviewed by the appropriate cognizant state agency.

Our objective was to determine whether the department reviewed the assigned subrecipients' cost allocation plans.

We tested a nonstatistical sample of subrecipients' cost allocation plans that had been assigned to the department for review and/or approval to determine if the plans had been reviewed and/or approved.

Based on our interviews and testwork, the department had not reviewed or approved subrecipients' cost allocation plans, as disclosed in finding 7.

Finding, Recommendation, and Management's Comment

7. Subrecipients' cost allocation plans were not properly reviewed

Finding

The Department of Health did not review subrecipients' cost allocation plans, in accordance with Department of Finance and Administration Policy 03. These cost allocation plans were allocating both indirect and multi-program expenditures during the year ended June 30, 2000. Testwork of 25 subrecipients' cost allocation plans revealed the following exceptions with 11 plans:

- Six cost allocation plans tested (24%) were not reviewed or approved by the department by November 29, 2000.
- Three approved cost allocation plans tested (12%) were not approved before June 30, 2000. They were approved 10 to 104 days after June 30, 2000.
- Two approved cost allocation plans tested (8%) did not include organizational charts. The department did not request the required organizational charts.

Department of Finance and Administration Policy 03, paragraph 16, states, "The cognizant state agency shall be responsible for approval of the cost allocation plan of the grantee." Paragraph 17 further states, "The plan should include an organizational chart." Without the allocation plans being approved, the subrecipients are using an unauthorized method to allocate indirect and multi-program expenditures that contracted state departments are reimbursing.

Recommendation

The Accounting Manager in Fiscal Services should review or approve the cost allocation plans during the fiscal year in which they are being applied and should also ensure that the cost allocation plans include all the required supporting information.

Management's Comment

We concur. The Contract Section within the Division of Fiscal Services will review and approve the subrecipients' cost allocation plans in the applicable fiscal year and ensure that the cost allocation plans include all the required supporting information.

CASH RECEIPTING PROCEDURES – SOUTH CENTRAL REGIONAL OFFICE

We were informed of a possible misappropriation of funds at the South Central Regional Office. Our investigation determined that \$727 had been misappropriated by an accountant at the regional office. The Department of Health terminated the employee. We referred the matter to the District Attorney General of the Twenty-second Judicial District (Maury County). As a part of our investigation, we reviewed the internal control for cash receipts at the regional office. The objective of our review was to determine whether the misappropriation of funds was the result of inadequate internal control.

We reviewed the office's assignment of duties and reconciliation procedures between receipts and deposits. The review included examinations of relevant documents and interviews with department personnel, supervisory staff, and management.

Based on our review, it appears that the South Central Regional Office had an adequate segregation of duties. However, as discussed in finding 8, the regional office did not have an adequate reconciliation process.

Finding, Recommendation, and Management's Comment

8. The South Central Regional Office does not have a reconciliation process to ensure that funds received are deposited, and resulting losses were not promptly reported

Finding

The South Central Regional Office does not reconcile cash receipts with bank deposits. As a result, \$727 was misappropriated by an employee, and the loss was not immediately detected.

Payments to the regional office that are made in person include both cash and checks and are received at clinics and by environmentalists. Payments received through the mail consist primarily of checks. Except for payments received through the mail, receipts are written when funds are received. Mail receipts are opened by the office supervisor, who records them on a check log. Both cash and checks are then forwarded to an accountant for deposit. After the deposit is made, the accountant is to forward the certification of deposit, which serves as a deposit slip, to the office supervisor to be posted to the accounting system. However, no one is comparing the certifications of deposit to the cash receipts or the check logs. Such a reconciliation process is an essential control needed to verify that receipts are deposited.

It appears this situation exists because management at the regional office has not assessed the risk of fraud and therefore has not properly designed control procedures.

The misappropriation was eventually discovered when an environmentalist requested copies of some certifications of deposit to reconcile his collection of permit fees to recorded

revenues. At this point, the department did not immediately notify the Comptroller of the Treasury of the misappropriation as required by *Tennessee Code Annotated*. Section 8-19-501, *Tennessee Code Annotated*, states:

It is the duty of any official of any agency of the state having knowledge of shortages of moneys of the state, or unauthorized removal of state property, occasioned either by malfeasance or misfeasance in office of any state employee, to report the same immediately to the comptroller of the treasury.

Instead, the department waited over six months to report this matter to the Comptroller.

The purpose of the statutory requirement to notify the Comptroller is to ensure a thorough investigation and an appropriate resolution in the best interest of the state.

Recommendation

The office supervisor or someone other than the employee who prepares deposits should reconcile certifications of deposit with the cash receipts and check logs. Any discrepancies should be investigated immediately and resolved. Management should ensure that misappropriations are reported to the Comptroller immediately.

Management's Comment

We concur and have changed our internal process. In November 1999 the office supervisor, who has no responsibility for receipting and depositing funds, began reconciling the certificates of deposit to the cash receipts (a printout of the Patient Tracking, Billing, and Management Information System [PTBMIS]) and the check log. Also, a revenue route slip was developed to track money from collection to deposit.

The Office of Audit and Investigations has developed written procedures for reporting suspected employee misconduct in collaboration with fiscal officials within the Department of Health, the Department of Mental Health and Developmental Disabilities, the Division of Mental Retardation, and the Bureau of TennCare. Implementation of these procedures is scheduled for February 2001, and should ensure compliance with *Tennessee Code Annotated*, Section 8-19-501. As of September 2000, the Office of Audit and Investigations began logging suspected employee misconduct resulting in a loss of state resources reported by the four entities. These matters have been immediately reported to the Division of State Audit.

OBSERVATIONS AND COMMENTS

TITLE VI OF THE CIVIL RIGHTS ACT OF 1964

Section 4-21-901, *Tennessee Code Annotated*, requires each state governmental entity subject to the requirements of Title VI of the Civil Rights Act of 1964 to submit an annual Title VI compliance report and implementation plan to the Department of Audit by June 30, 1994, and each June 30 thereafter. The Department of Health filed its compliance report and implementation plan on June 29, 2000.

Title VI of the Civil Rights Act of 1964 is a federal law. The act requires all state agencies receiving federal money to develop and implement plans to ensure that no person shall, on the grounds of race, color, or origin, be excluded from participation in, be denied the benefits of, or be subjected to discrimination under any program or activity receiving federal funds.

On October 15, 1998, the Commissioner of Finance and Administration notified all cabinet officers and agency heads that the Human Rights Commission is the coordinating state agency for the monitoring and enforcement of Title VI.

A summary of the dates state agencies filed their annual Title VI compliance reports and implementation plans is presented in the special report *Submission of Title VI Implementation Plans*, issued annually by the Comptroller of the Treasury.

TENNCARE ELIGIBILITY – BRADLEY COUNTY HEALTH DEPARTMENT

During the audit it was determined that on July 9, 1999, the Office of Audit and Investigations with the Department of Health had received information that a TennCare Clerk with the Bradley County Health Department had committed fraud and forgery in submitting several TennCare applications. The results of the review disclosed that she had filed TennCare applications for herself; her husband, who was in jail at the time; and a friend. The TennCare application review process rejected the husband's application because TennCare staff determined that he was in jail at the time, and thus not eligible. However, the applications for the clerk and her friend were accepted because the clerk had falsified the related supporting documentation for those applications. Her falsified documentation included forged signatures. To conceal her actions, the clerk did not record the applications for TennCare on the TennCare enrollment log maintained at the Bradley County Health Department.

The state paid capitation fees for the clerk and her friend totaling \$1,662.08 before their ineligible status was discovered. This matter was properly referred for prosecution, which is still pending. However, the department's failure to promptly notify this office, as required by statute, was reported as a finding as a part of the audit of the Department of Finance and Administration for the year ended June 30, 2000. Management's failure to promptly notify this office in

accordance with Section 8-19-501, *Tennessee Code Annotated*, is also mentioned in finding 8 of this report. Management concurred with both findings and stated that written procedures have been developed, and this office is immediately being notified as required by statute.

APPENDIX

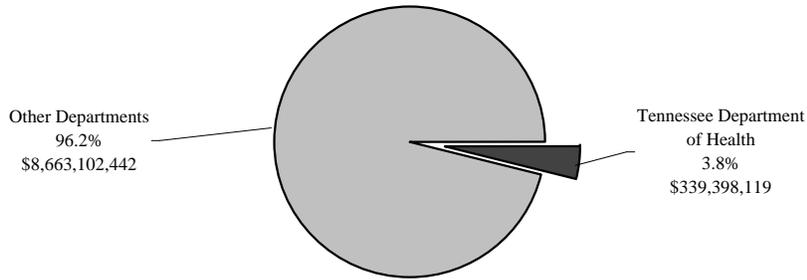
DIVISIONS AND ALLOTMENT CODES

Department of Health divisions and allotment codes:

- 343.01 Executive Administration
- 343.03 Office of Budget and Finance
- 343.04 Bureau of Information Systems
- 343.05 Bureau of Health Licensure and Regulation
- 343.07 Emergency Medical Service
- 343.08 Laboratory Services
- 343.10 Health Related Boards
- 343.39 Division of General Environmental Health
- 343.44 Bureau of Alcohol and Drug Abuse Services
- 343.45 Health Services Administration
- 343.47 Maternal and Child Health
- 343.49 Communicable and Environmental Disease Services
- 343.52 Population-Based Services
- 343.53 WIC Supplemental Foods
- 343.60 Local Health Services
- 343.70 Nursing Home Grant Assistance Program

General Fund Expenditures

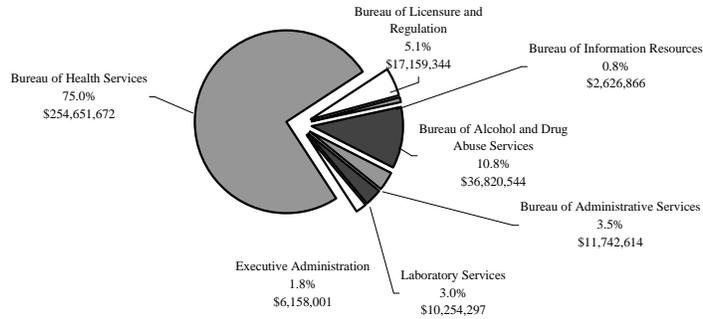
Fiscal Year Ended June 30, 2000 (Unaudited)



Source: Department of Health

Expenditures by Allotment and Division

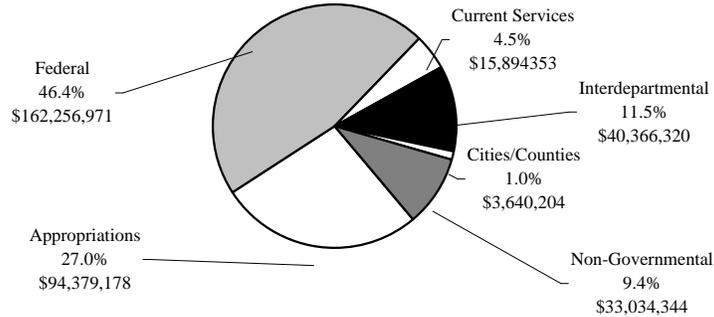
Fiscal Year Ended June 30, 2000 (Unaudited)



Source: Department of Health

Department of Health Funding Sources

Fiscal Year Ended June 30, 2000 (Unaudited)



Source: Department of Health